REPORT OF EXAMINATION
OF THE

AMERICAN EQUITY SPECIALTY
INSURANCE COMPANY

AS OF
DECEMBER 31, 2006

Participating State
and Zone:

California

Filed June 24, 2008

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Los Angeles, California
May 15, 2008

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition (EX4) Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable Kent Michie
Secretary, Zone IV-Western
Commissioner of Insurance
Department of Insurance, State of Utah
Salt Lake City, Utah

Honorable Steve Poizner
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman, Secretary, and Commissioner:

Pursuant to your instructions, an examination was made of the

AMERICAN EQUITY SPECIALTY INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 385 Washington Street, St. Paul, Minnesota 55102. During the period covered by this examination, the Company's statutory home office was One Tower Square, Hartford Connecticut 01683. As noted in the "Subsequent Events" section of this report, the Company is no longer a California domiciled entity.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2002. This examination covers the period from January 1, 2003 through December 31, 2006. The examination was made pursuant to the National Association of Insurance Commissioners' plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2006 as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; accounts and records and sales and advertising.

SUBSEQUENT EVENTS

Effective July 31, 2007, the Company redomiciled to the State of Connecticut.

COMPANY HISTORY

Effective August 20, 2002, the ultimate controlling entity of The Northland Company Insurance Group, which includes the Company, changed from Citigroup, Inc. to Travelers Property Casualty Corporation (TPCC). On April 1, 2004, TPCC completed its previously announced merger with the St. Paul Companies, forming The St. Paul Travelers Companies, Inc. Effective February 27, 2007, the name St. Paul Travelers Companies, Inc was changed to The Travelers Companies, Inc.

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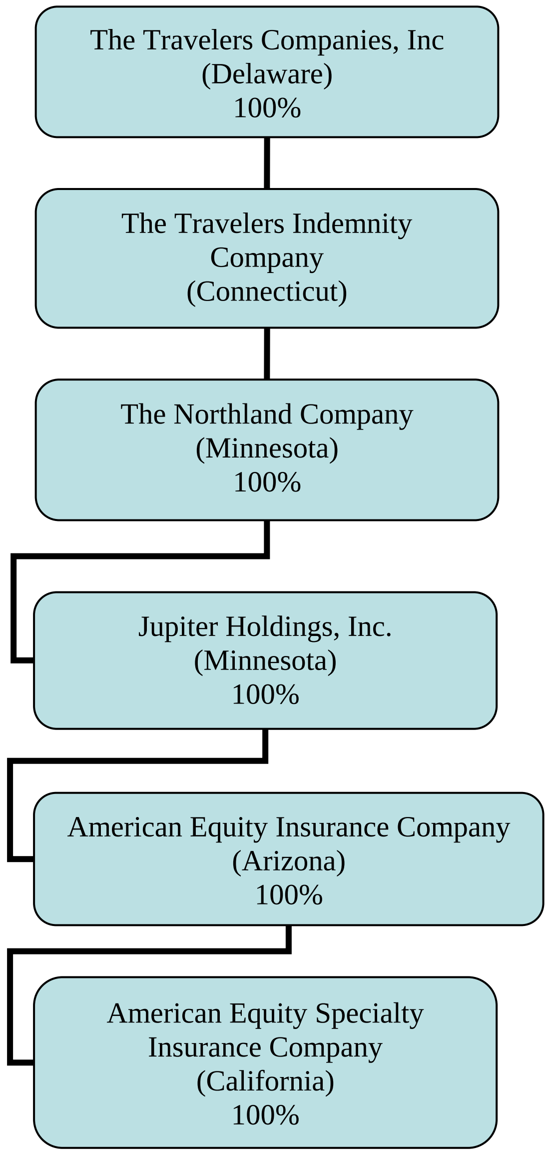
MANAGEMENT AND CONTROL

Ultimate control of the Company is maintained by The Travelers Companies, Inc. The following abbreviated organizational chart depicts the Company's relationship within the holding company system as of December 31, 2006:


The Travelers Companies, Inc
(Delaware)
100%
The Travelers Indemnity
Company
(Connecticut)
The Northland Company
(Minnesota)
100%
Jupiter Holdings, Inc.
(Minnesota)
100%
American Equity Insurance Company
(Arizona)
100%
American Equity Specialty
Insurance Company
(California)
100%

Management of the Company is vested in a five-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2006 follows:

Directors

Name and Residence	Principal Business Affiliation
Jay S. Benet Long Point, Connecticut	Chief Financial Officer The Travelers Companies, Inc.
William H. Heyman New York, New York	Chief Investment Officer The Travelers Companies, Inc.
Joseph P. Lacher, Jr. Glastonbury, Connecticut	Executive Vice President – Personal Insurance The Travelers Companies, Inc.
Brian W. MacLean Vernon, Connecticut	Chief Operating Officer The Travelers Companies, Inc.
Doreen Spadorcia Avon, Connecticut	Executive Vice President – Claim Services The Travelers Companies, Inc.

Principal Officers

Name	Title
Brian W. MacLean	President and Chief Executive Officer
Douglas K. Russell	Treasurer
Bruce A Backberg	Corporate Secretary

Management Agreements

Expense Allocation Agreement: In conjunction with the merger of Travelers Property Casualty Corp. and The St. Paul Companies, Inc., a revised expense allocation agreement was formulated to set forth the methodology by which services are provided and expenses are allocated and to include the additional insurers within The St. Paul Travelers Companies, Inc. group of companies. In accordance with the agreement, The Travelers Indemnity Company will provide or obtain services and incur costs on behalf of the other parties. Services will include but are not limited to financial management, operational management, accounting, treasury, payroll, internal audit, human resource management, benefit services, risk management, legal, investment management and advisory, claim administration, billing and collection, and business processing. Reimbursement is on a cost basis with no profit component. The agreement was approved by the California Department of Insurance(CDI) on March 12, 2007.

Consolidated Federal Income Tax Agreement: An amended and restated tax allocation agreement was also executed at the same time to reflect the inclusion of affiliates from both merger parties. Accordingly, for the taxable years ending after April 1, 2004, the renamed common parent, The Travelers, Companies, Inc., began to file a consolidated federal income tax return on behalf of the participants, including the Company. The Company's allocated tax liability is predicated upon the amount that it would be liable for under a separate filing. The agreement was approved by the CDI on May 27, 2004.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2006, the Company was licensed to transact multiple lines of property and casualty insurance in the following 39 states and the District of Columbia:

Arkansas	Iowa	Nebraska	Tennessee
California	Kansas	Nevada	Texas
Colorado	Kentucky	North Dakota	Utah
Connecticut	Maine	Ohio	Vermont
Florida	Maryland	Oklahoma	Virginia
Georgia	Michigan	Oregon	Washington
Hawaii	Minnesota	Pennsylvania	West Virginia
Idaho	Mississippi	Rhode Island	Wisconsin
Illinois	Missouri	South Carolina	Wyoming
Indiana	Montana	South Dakota	

The Company specializes in trucking commercial liability and physical damage coverages. During 2006, the Company wrote $9.6 million of direct premiums. Of the direct premiums written, less than 1% pertained to California risks. Business is produced through a limited network of general and selected specialty retail agents.

REINSURANCE

Intercompany Pooling Agreement

During the period under review, the Company and six of its affiliates were participants in the Northland Pool. The lead company in the Northland Pool was Northland Insurance Company, a Minnesota domiciled entity. All underwritten risks were pooled and then assumed on a proportionate basis with the Company maintaining a 2% participation interest.

Effective October 1, 2007, the Northland Pool was dissolved whereupon the Company became a member (retroactive to January 1, 2007) of the Travelers Reinsurance Pool with a 10% participation interest. The Travelers Indemnity Company is the lead company in the aforementioned pool.

In conjunction with the aforementioned intercompany pooling agreement, the Company was also party to an intercompany management agreement during the examination period. This agreement provided for the allocation of all underwriting pool costs between the participants on the basis of participation interest. This agreement was also terminated on October 1, 2007 retroactive to January 1, 2007.

Assumed

Aside from its participation in the above referenced Northland Pool, the Company has not assumed reinsurance during the period under examination.

Ceded

Since 2002, the Company has not ceded reinsurance.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2006

Underwriting and Investment Exhibit for the Year Ended December 31, 2006

Reconciliation of Surplus as Regards Policyholders
from December 31, 2002 through December 31, 2006

Statement of Financial Condition
as of December 31, 2006

Assets	Ledger and Nonledger Assets	Assets Not Admitted	Net Admitted Assets	Notes
Bonds	$ 35,202,046	$	$35,202,046	
Cash and short-term investments	7,114,842		7,114,842	
Investment income due and accrued	448,295		448,295	
Uncollected premiums and agents' balances in course of collection	1,324,525	73,177	1,251,348	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	2,037,219		2,037,219	
Amounts recoverable from reinsurers	(340)		(340)	
Net deferred tax asset	1,211,791	562,333	649,458	
Aggregate write-ins for other than invested assets	43,727		43,727	
Total assets	$ 47,382,105	$ 635,510	$46,746,595	

Liabilities, Surplus and Other Funds				
Losses			$13,190,793	(1)
Loss adjustment expenses			3,568,462	(1)
Commissions payable, contingent commissions and other similar charges			291,809	
Other expenses			187,308	
Taxes, licenses and fees			102,039	
Current federal and foreign income taxes			681,706	
Unearned premiums			5,855,127	
Ceded reinsurance premiums payable			74,138	
Amounts withheld or retained by company for account of others			206,745	
Provision for reinsurance			207,262	
Drafts outstanding			1,815	
Payable to parent, subsidiaries and affiliates			168,493	
Aggregate write-ins for liabilities			(97,660)	
Total liabilities			24,438,037	
Aggregate write-ins for special surplus funds		$ 121,150		
Common capital stock		3,500,000		
Gross paid-in and contributed surplus		16,000,000		
Unassigned funds (surplus)		2,687,408		
Surplus as regards policyholders			22,308,558	
Total liabilities, surplus and other funds			$46,746,595	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2006

Statement of Income

Underwriting Income		
Premiums earned		$13,968,088
Deductions:		
Losses incurred	$7,210,073	
Loss expenses incurred	1,253,278	
Other underwriting expenses incurred	4,336,720	
Total underwriting deductions		12,800,071
Net underwriting gain		1,168,017
Investment Income		
Net investment income earned	$1,706,006	
Net realized capital losses	(4,055)	
Net investment gain		1,701,951
Other Income		
Net loss from agents’ balances charged off	$ (89,594)	
Finance and service charges not included in premiums	191,403	
Aggregate write-ins for miscellaneous losses	121,573	
Total other income		223,382
Net income before federal and foreign income taxes		3,093,350
Federal and foreign income taxes incurred		774,709
Net income		$ 2,318,641

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2005		$18,237,165
Net income	$ 2,318,641	
Change in net deferred income tax	10,278	
Change in nonadmitted assets	(5,007)	
Change in provision for reinsurance	1,747,481	
Change in surplus as regards policyholders		4,071,393
Surplus as regards policyholders, December 31, 2006		$22,308,558

Reconciliation of Surplus as Regards Policyholders
from December 31, 2002 through December 31, 2006

	Gain in Surplus	Loss in Surplus	
Surplus as regards policyholders, December 31, 2002, per Examination			$ 10,059,091
Net income	$ 6,226,648	$	
Change in net deferred income tax		271,038	
Change in nonadmitted assets	165,508		
Change in provision for reinsurance	4,628,349		
Surplus adjustments: Paid-in	1,500,000		
Totals	$ 12,520,505	$ 271,038	
Net increase in surplus as regards policyholders			12,249,467
Surplus as regards policyholders, December 31, 2006, per Examination			$ 22,308,558

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

For the purpose of assessing the reasonableness of The Northland Company Insurance Groups' loss and loss adjustment expense reserves, the Minnesota Department of Insurance, which maintains regulatory responsibility for the lead company within the group, retained the services of a consulting actuary. Based on the analysis by the consulting actuary, the Company's combined reserves for losses and loss adjustment expenses as of December 31, 2006 were determined to be reasonably stated and have been accepted for purposes of this examination report.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

There are no recommendations in the current report.

Previous Report of Examination

Corporate Records (Page 6): In accordance with the requirements of California Insurance Code (CIC) Section 735, it was recommended that the board of directors review and acknowledge during its next regular meeting the prior Report of Examination issued by the California Department of Insurance. Subsequent board minutes reflect a formal acknowledgement of the receipt and review of the 1999 and 2002 Reports of Examination.

Accounts and Records (Page 10): In accordance with the requirements of CIC Section 734, it was recommended that the Company maintain its own copies of all pool related working papers. The Company was found to be in compliance with the recommendation.

Bonds and Cash and Short-Term Investments (Page 16): It was recommended that the Company comply with CIC Section 1104.9**.** The Company is currently in compliance with the recommendation.

Premiums and Agents' Balances in Course of Collection (Page 16): It was recommended that the Company implement procedures to insure compliance with Statements of Statutory Accounting Principles (SSAP) No. 6. The Company was found to be in compliance with SSAP No. 6.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

______/S/__________________

David A. Fischman, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California